

Cinergy Corp.
139 East Fourth Street
P.O. Box 960
Cincinnati, OH 45201-0960

VIA OVERNIGHT MAIL

CINERGY®

July 29, 2004

Ms. Elizabeth O'Donnell
Executive Director
Public Service Commission
211 Sower Boulevard
P. O. Box 615
Frankfort, Kentucky 40602

RECEIVED

JUL 30 2004

**PUBLIC SERVICE
COMMISSION**

Re: In the Matter of the Application of The Union Light, Heat and Power Company for Deviation from the Requirements of KRS 278.2207(1)(b) to Permit Winter 2004 Natural Gas Purchases from Cinergy Marketing & Trading, LP, an Affiliate Case No. 2004-00301

Dear Ms. O'Donnell:

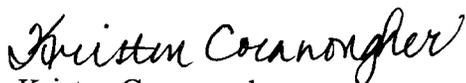
Enclosed please find a signed original, 12 redacted copies and one sealed un-redacted copy of the Application of the Union Light, Heat and Power Company for Deviation from the Requirements of KRS 278.2207(1)(b) as stated in the above-referenced caption.

Also enclosed are a signed original and 12 copies of the Petition of The Union Light, Heat and Power Company for Confidential Treatment of Information.

Please date and file-stamp the two extra copies of both filings and return them in the overnight envelope provided.

If you have any questions, please do not hesitate to contact me at (513) 287-1981.

Sincerely,


Kristen Cocanaugher
Paralegal

KC/sew
Enclosures

COMMONWEALTH OF KENTUCKY

BEFORE THE KENTUCKY PUBLIC SERVICE COMMISSION

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JUL 30 2004

**PUBLIC SERVICE
COMMISSION**

In the Matter of:

APPLICATION OF THE UNION LIGHT, HEAT)
AND POWER COMPANY FOR DEVIATION)
FROM THE REQUIREMENTS OF KRS)
278.2207(1)(b) TO PERMIT WINTER 2004)
NATURAL GAS PURCHASES FROM)
CINERGY MARKETING & TRADING, LP,)
AN AFFILIATE)

CASE NO. 2004-00301

PETITION OF THE UNION LIGHT, HEAT
AND POWER COMPANY FOR
CONFIDENTIAL TREATMENT OF INFORMATION

The Union Light, Heat and Power Company (ULH&P), pursuant to 807 KAR 5:001, Section 7, respectfully requests the Commission to classify and protect as confidential certain information that is contained in its Application in this proceeding, which is being filed contemporaneously with this petition. In support thereof, ULH&P states:

1. ULH&P has filed today documents containing information solicited by ULH&P for its winter gas supply procurement process. It contains the bidders' pricing, the public disclosure of which would damage ULH&P's and the bidders' competitive position and business interests, and would also damage ULH&P by making it more difficult to obtain bidders for future gas supply. As required by 807 KAR 5:001, Section 7(2)(b), ULH&P is providing one copy of the bid information under seal.

2. The Kentucky Open Records Act exempts from disclosure certain commercial information. KRS 61.878 (1)(c). To qualify for this exemption and, therefore, maintain the confidentiality of the information, a party must establish that disclosure of the commercial information would permit an unfair advantage to competitors of that party.

3. The bid information described above contains sensitive pricing information, the disclosure of which would injure ULH&P and the aforementioned bidders solicited by ULH&P and their competitive position and business interests. ULH&P's bid process is confidential. Public release of this information would allow other suppliers to have access to the bid information and would likely discourage suppliers whose information is contained in the confidential material from bidding on similar RFPs because the disclosure of their prices would put them at a competitive disadvantage with their competitors. These competitors would have access to this information while those suppliers whose information is contained in the confidential material would not have access to such information regarding the other suppliers. Similar information has been treated as confidential in Case No. 2002-375, which relates to a similar transaction.

4. The bid information described above contains the following categories of information, which are commercially sensitive: the terms at which certain suppliers bid to supply gas to ULH&P.

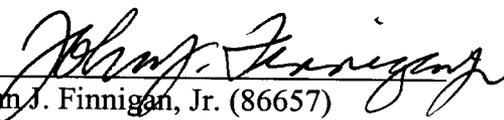
5. The information for which ULH&P is seeking confidential treatment is not known outside of ULH&P and its bidders, and it is not disseminated within ULH&P

except to those employees with a legitimate business need to know and act upon the information.

6. The public interest will be served by granting this Petition, in that competition among ULH&P's prospective gas suppliers will be fostered and the cost of gas to ULH&P's customers will thereby be minimized.

WHEREFORE, The Union Light, Heat and Power Company respectfully requests that the Commission classify and protect as confidential the specific information described herein.

Respectfully submitted,



John J. Finnigan, Jr. (86657)
Senior Counsel
The Union Light, Heat and
Power Company
2500 Atrium II
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Cincinnati, Ohio 45201-0960
(513) 287-3601

COMMONWEALTH OF KENTUCKY

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BEFORE THE PUBLIC SERVICE COMMISSION

JUL 30 2004

In the Matter of:

**PUBLIC SERVICE
COMMISSION**

APPLICATION OF THE UNION LIGHT, HEAT)	CASE NO.
AND POWER COMPANY FOR DEVIATION)	2004- <u>00301</u>
FROM THE REQUIREMENTS OF KRS)	
278.2207(1)(b) TO PERMIT WINTER 2004-2005)	
NATURAL GAS PURCHASES FROM)	
CINERGY MARKETING & TRADING, LP,)	
AN AFFILIATE)	

APPLICATION

Pursuant to KRS 278.2207(2), The Union Light, Heat and Power Company (ULH&P) requests that the Commission grant a deviation from the requirements of KRS 278.2207(1)(b) to allow ULH&P to purchase natural gas during the winter of 2004-2005 from Cinergy Marketing & Trading, LP (CM&T), an affiliate, at the terms and conditions stated in the accompanying memorandum, for the reasons stated in the memorandum. ULH&P also requests that the Commission make a finding that such purchases are at arm's length, such that the purchases comply with KRS 278.2213(6) or, in the alternative, ULH&P also requests that the Commission also grant a deviation from the requirements of this statute.



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 Senior Counsel
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MEMORANDUM IN SUPPORT OF
APPLICATION FOR DEVIATION

A. Pricing Requirements for Affiliate Transactions

Kentucky Revised Statutes 278.2207(1)(b) requires that products and services sold by an affiliate to a utility must be priced at the affiliate's fully distributed cost but in no event greater than market or in compliance with the utility's existing USDA, SEC, or FERC-approved cost allocation methodology.

B. Applicability of KRS 278.2207(1)(b) to this Transaction

ULH&P desires to purchase natural gas from CM&T, under the terms stated herein, for re-sale to ULH&P's native load customers. ULH&P is a utility as defined in KRS 278.010. CM&T is an affiliate of ULH&P, engaged in the business of marketing natural gas and electricity. The pricing for this transaction therefore must comply with KRS 278.2207(1)(b), unless a deviation is granted.

The transaction is not priced at CM&T's fully distributed cost because natural gas is a commodity, and CM&T, as a marketer, sells natural gas at the market price. The transaction is not priced pursuant to ULH&P's existing SEC and FERC-approved cost allocation methodologies because these cost allocation methodologies do not apply to commodity transactions. ULH&P therefore can purchase natural gas from CM&T only if the Commission grants a deviation pursuant to KRS 278.2207(2).

C. Terms of the Transaction for Which ULH&P Seeks Deviation

ULH&P requests a deviation to purchase natural gas from CM&T for the winter of 2004-2005 under the following terms and conditions:

Location: Columbia Gulf, Onshore
Type: Base load
Price: [REDACTED]
Reservation Fee: [REDACTED]
Volumes: [REDACTED] for November 1, 2004 – March 31, 2005

Location: Tennessee, 500 Leg
Type: Daily Swing
Price: [REDACTED]
Reservation Fee: [REDACTED]
Volumes: [REDACTED]

D. Background for Base Load Transaction

On May 14, 2004 ULH&P initiated a competitive bidding process to obtain part of its winter 2004-2005 gas supply to be priced on a “cost-averaged” basis, in accordance with ULH&P’s gas hedging plan, approved by the Commission in Case No. 2003-00151. ULH&P telephoned three suppliers to request bids for gas supply for [REDACTED]/day for the 2004-2005 winter season for ULH&P. In order to obtain apples-to-apples bids, the suppliers were asked to submit their bids for firm base load supply on a cost-averaged basis, for delivery at Columbia Gulf Onshore. The cost-averaged price is to be determined based on the average NYMEX closing price for winter strip purchases from June 1, 2004 through October 27, 2004.

ConocoPhillips, Occidental and CM&T were contacted for bids based on their familiarity with cost-averaging, willingness to structure similar deals in the past, and having a financial

condition that would make them acceptable counterparties. The average NYMEX price is the same regardless of supplier, so the only way to differentiate the suppliers' bids is the basis charged by the supplier for delivery at Columbia Gulf Onshore. The bid results were as follows:

<u>Bidder</u>	<u>Amount of Bid</u>
ConocoPhillips	██████████
Occidental	██████████
CM&T	██████████

Given the volume of ██████████ during the winter season, CM&T's bid would save ULH&P's customers ██████████ over Occidental's bid, and ██████████ over ConocoPhillips' bid during the term of the agreement.

E. Background for Swing Transaction

On June 11, 2004 ULH&P initiated a competitive bidding process to obtain its winter 2004-2005 gas supply. ULH&P e-mailed invitations to participate in the request for proposal (RFP) utilizing Pantellos RFX, an internet based tool for soliciting bids. ULH&P requested bids on firm contracts for gas supply for the 2004-2005 winter season and also for longer term contracts up to two years. In order to obtain apples-to-apples bids, the suppliers were asked to submit their bids for firm base load supply at the *Inside FERC First of Month Index (FOMI)* price. The bids for firm swing load supply were requested at the *Gas Daily* midpoint price. A copy of the RFP, and the invitation letter to the producers and marketers to whom the RFP was sent, is at Attachment A.

The invitation to participate in the RFP was sent to 17 producers and marketers, which were regarded as among the industry gas supply leaders, and whose financial condition would have made them acceptable counterparties. Ten potential suppliers submitted bids in response to the RFP and all of the bids included a reservation fee. A summary of the bids is included in Attachment B. Cinergy's Gas Commercial Operations Department utilized an optimization model to evaluate the various bids received from suppliers and to allocate the natural gas requirements among several suppliers so as to minimize the total reservation fees, subject to certain criteria.

In addition to considering reservation fees, ULH&P is typically concerned with qualitative measures, such as whether the supplier is a producer or marketer, the supplier's credit rating and the supplier's past performance.

The optimal mix of suppliers for the winter of 2004-05 included CM&T, which offered the second lowest reservation fee for daily swing at Tennessee 500 Leg. Attachment C is a chart listing ULH&P's choice of five suppliers, and the amounts of the reservation fees that these suppliers proposed to charge. Excluding CM&T from the supply portfolio would necessitate purchasing the Tennessee swing supply from Sequent, which bid a reservation fee of [REDACTED] and a commodity price of [REDACTED]. The resulting costs would be from [REDACTED] to [REDACTED] higher, depending on the load factor.

F. Deviation is in Public Interest

ULH&P respectfully submits that the deviation is in the public interest and should be granted. As a result of the competitive bidding process described above, ULH&P determined that it would have to obtain gas from CM&T in the volumes and at the prices described above, in

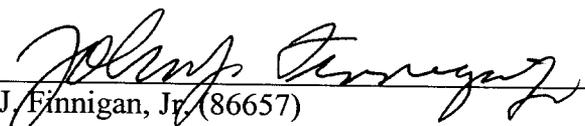
order to obtain the optimal prices and supplier mix for its gas needs for the winter of 2004-2005. Excluding CM&T from the supplier portfolio for both the cost averaging and the swing supply would result in additional costs of approximately [REDACTED] to [REDACTED]. As a result, ULH&P's customers would experience significant savings if the Commission approves this transaction.

G. Impact of KRS 278.2213(6)

KRS 278.2213(6) provides that all dealings between a utility and a non-regulated affiliate must be at arm's length. ULH&P submits that this transaction is at arm's length because: (1) the transaction was negotiated by separate employees of separate Cinergy affiliates; and (2) the employee who negotiated the transaction on behalf of ULH&P has the obligation to obtain gas for ULH&P's firm sales customers at the least cost. If, however, the Commission concludes that this transaction was not at arm's length, then ULH&P also requests a deviation from the requirements of this statute for this transaction.

CONCLUSION

Based on the foregoing, ULH&P respectfully requests that the Commission grant ULH&P's application for deviation as set forth herein. ULH&P respectfully requests that the Commission issue a ruling in this matter by September 1, 2004, as ULH&P will need to make alternative supply arrangements if Commission approval is not obtained by that date.


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Senior Counsel
The Union Light, Heat and Power Company
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June 11, 2004

Re: **Request for Proposal – Natural Gas Supply (Gas Operations)**

Dear Supplier:

The Cincinnati Gas & Electric Company (CG&E), The Union Light, Heat and Power Company (ULH&P) and Lawrenceburg Gas Company (jointly called Cinergy) are requesting bids from various natural gas suppliers to provide firm natural gas deliveries into interstate pipelines that serve Cinergy for the period November 1, 2004 through October 31, 2006. Cinergy is requesting both base and swing supply for distribution and pipeline storage injection.

Cinergy has implemented RFX, a web-based bid management system that makes it easier and more efficient to manage the Request For Proposal (RFP) process. You have been asked to join in this initiative by registering, completing and maintaining your business profile in order to receive web-based RFPs from Cinergy. Your submittals and transmissions are encrypted and completely secure and are visible only to Cinergy and yourself. There is no cost to you, the Supplier, to use the system as a Bidder. All bid responses, questions, and answers must be submitted using the RFX solution. If you need assistance, please contact Pantellos Support at 1-877-777-4888.

The attachments on-line at Pantellos' RFX website:

- Request for Proposal – Requesting gas Supplier (Seller) to provide firm base and swing supply, by local distribution company.
- Cinergy City Gate Delivery Map
- Consent to Assign – CG&E and ULH&P intend to assign all gas supplier contracts to an Asset Manager. Cinergy's current Asset Management Agreement with its affiliate, Cinergy Marketing & Trading, expires October 31, 2004.

Tuesday, June 15th, Pantellos will electronically send invitations to the RFX Event to the invited bidders. Proposals are to be submitted no later than 2 PM ECT, June 29, 2004.

Sincerely,

James P. Henning
Manager, Gas Commercial Operations

REQUEST FOR PROPOSAL

ATTACHMENT NO. 1

PAGE 2 OF 6

PURCHASER	The Union Light, Heat and Power Company (ULH&P)
SELLER	
PRODUCT	Firm Base and Swing Natural Gas volumes into interstate pipelines for delivery to city gate and/or pipeline storage injection
TERM	November 1, 2004 through October 31, 2006
RESERVATION CHARGE	\$0. _____ per dekatherm per day of base load on Tennessee Gas Pipeline \$0. _____ per dekatherm per day of base load on Columbia Gulf Transmission
COMMODITY PRICE	<p>Base Price: Inside FERC's Gas Market Report, "PRICES OF SPOT GAS DELIVERED TO PIPELINES", first publication of delivery month</p> <p>Swing Price: <input type="checkbox"/> Gas Daily Midpoint <input type="checkbox"/> Other _____</p> <p>Cinergy may direct Seller to enter into price caps, price floors, price collars, fixed basis differentials to NYMEX, or other pricing terms that are mutually agreed upon between Seller and Cinergy.</p>
NOMINATIONS	<i>Please specify any weekend/weekday, daily and intra-day nomination restrictions, and notification parameters</i>
WEEKEND/HOLIDAY/INTRADAY	<i>Please specify any additional premiums should CG&E desire to revise swing volumes during weekends/holidays/intraday.</i>

ULH&P Requirements

[volumes stated as dekatherms per day at the city gate]

PIPELINE	PIPELINE DELIVERY POINT	SUPPLY TYPE	11/1/04 - 03-31-05	11/1/04 - 10-31-05	11/1/04 - 03-31-06	11/1/04 - 10-31-06
Tennessee	500 leg	Firm Base	up to			
		Firm Swing				
Columbia Gulf	south La. onshore	Firm Base	up to			
		Firm Swing				

Seller Proposal

PIPELINE	PIPELINE DELIVERY POINT	SUPPLY TYPE	11/1/04 - 03-31-05	11/1/04 - 10-31-05	11/1/04 - 03-31-06	11/1/04 - 10-31-06
Tennessee		Firm Base				
		Firm Swing				
Columbia Gulf		Firm Base				
		Firm Swing				

CONTRACT ASSIGNMENT	ULH&P plans to assign Seller's gas supply agreement with ULH&P to its Asset Manager effective November 1, 2004 (please see 'Consent to Assign' letter).
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Re: Consent to Assign

The Cincinnati Gas & Electric Company and The Union Light, Heat and Power Company (jointly called Cinergy) intends to assign certain of its rights and obligations under its Base Contract for Sale and Purchase of Natural Gas (the "Agreement") with _____ to its Asset Manager effective November 1, 2004.

This letter shall serve as written consent by _____ to the assignment under Section 14.1 of the Agreement. Pursuant to Section 14.1, despite such assignment by Cinergy to its Asset Manager, Cinergy shall remain principally liable for and shall not be relieved of or discharged from any obligations under the Agreement.

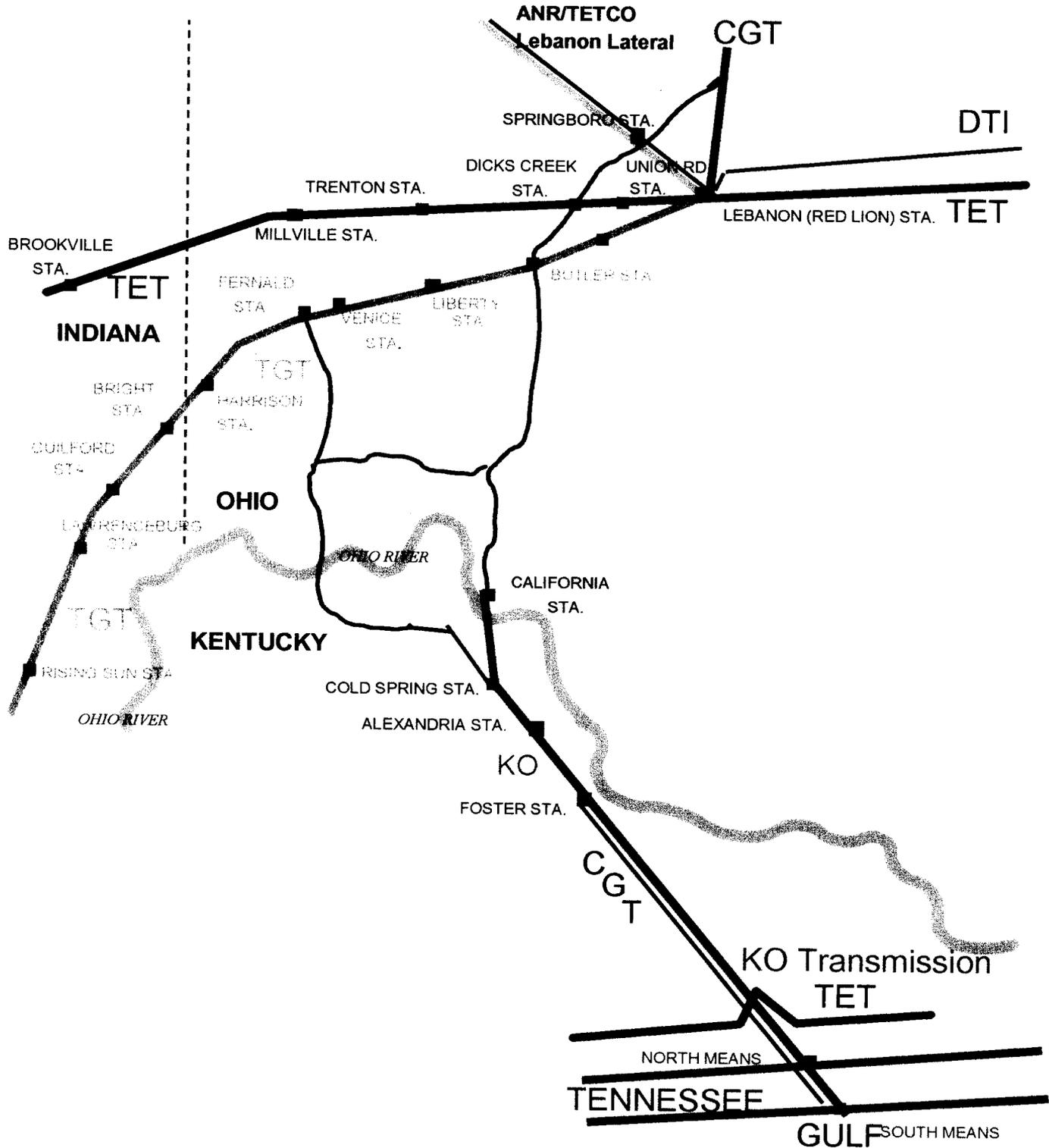
Supplier: _____

Signature: _____

Printed Name: _____

Date: _____

City Gate Station Map



The Union Light Heat & Power Company
Gas Commercial Operations
Supplier Bid Summary

	Anadarko	BP	Chevron	Conoco	ExxonMobil	CoEnergy	CM&T	Occidental	Oneok	Sequent
5 Months (11/04-3/05)										
Columbia Gulf										
Base Reservation	-									
Swing Reservation	-									
Swing Commodity	-									
Tennessee										
Base Reservation										
Swing Reservation										
Swing Commodity										
12 Months (11/04 - 10/05)										
Columbia Gulf										
Base Reservation	-									
Swing Reservation	-									
Swing Commodity	-									
Tennessee										
Base Reservation										
Swing Reservation										
Swing Commodity										
17 Months (11/04 - 3/06)										
Columbia Gulf										
Base Reservation	-									
Swing Reservation	-									
Swing Commodity	-									
Tennessee										
Base Reservation										
Swing Reservation										
Swing Commodity										
24 Months (11/04 - 10/06)										
Columbia Gulf										
Base Reservation	-									
Swing Reservation	-									
Swing Commodity	-									
Tennessee										
Base Reservation										
Swing Reservation										
Swing Commodity										
Swing Type	Keypwhole	Gas Daily	Gas Daily	Gas Daily	No Swing	Gas Daily	Gas Daily	Gas Daily	Gas Daily	Gas Daily
Other		8:30 Norm	8:30 or 9:00 Norm?		Base only for 1 year					

The Union Light Heat & Power Company
Gas Commercial Operations
Supply Portfolio - November 2004 - March 2005
Reservation Fees

	Dth per Day					Total Volume	Reserv. Fee	Total Cost
	<u>Nov</u>	<u>Dec</u>	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>			
Anadarko								
Tennessee Base								
Tennessee Swing								
Total								
Conoco								
Columbia Base								
Columbia Base								
Tennessee Base								
Total								
CoEnergy								
Columbia Base								
Columbia Swing								
Total								
Occidental								
Columbia Base								
Tennessee Swing								
Total								
CM&T								
Columbia Base								
Tennessee Swing								
Total								
Total Winter Firm Supply Reservation Charges								

(1) As part of ULH&P's Hedging Strategy, volumes have been hedged with Conoco/Phillips, Occidental and CM&T prior to locking in firm supply for the winter, so no reservation fee applies.